

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Order Instituting Investigation Into the Gas Market Activities of Southern California Gas Company, San Diego Gas and Electric, Southwest Gas, Pacific Gas and Electric, and Southern California Edison and Their Impact on the Gas Price Spikes Experienced at the California Border from March 2000 through May 2001.

Investigation 02-11-040  
(Filed November 21, 2002)

Order Instituting Investigation Whether San Diego Gas & Electric Company, Southern California Gas Company and Their Holding Company, Sempra Energy, Respondents, Have Complied With Relevant Statutes and Commission Decisions, Pertaining to Respondents' Holding Company Systems and Affiliate Activities.

Investigation 03-02-033  
(Filed February 27, 2003)

**SCOPING MEMO FOR INVESTIGATION (I.) 03-02-033 AND  
ASSIGNED COMMISSIONER RULING REGARDING  
COORDINATION OF I.02-11-040 AND I.03-02-033**

**I. Summary**

A prehearing conference (PHC) was held jointly in I.02-11-040 and I.03-02-033 on March 3, 2006.<sup>1</sup> Because of the need for further discussion regarding coordination of the two proceedings, the PHC was continued to

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<sup>1</sup> Other PHCs have been held previously in both I.02-11-040 and I.03-02-033.

March 7, 2006. San Diego Gas & Electric Company (SDG&E), Southern California Gas Company (SoCalGas), and Southern California Edison Company (SCE) filed PHC Statements in I.02-11-040 and I.03-02-033, and Sempra Energy (Sempra) filed a PHC Statement in I.02-11-040.

Pursuant to Article 2.5 of the Commission Rules of Practice and Procedure,<sup>2</sup> this ruling sets forth the scope and procedural schedule of I.03-02-033 and designates the principal hearing officer of that proceeding. As discussed at the March 3 and 7, 2006 PHC and addressed in more detail in this ruling, I.03-02-033 and Phase I of I.02-11-040 will be coordinated for the purpose of addressing affiliate activities, which are being investigated in both proceedings. Today's ruling addresses certain other procedural issues for the proceedings.

## **II. Background – I.02-11-040**

The Commission initiated I.02-11-040 on November 21, 2002 to investigate the gas market activities of California utilities and their impact on the natural gas spikes at the California border from March 2000 through May 2001 (the Subject Period). A Scoping Memo was issued for Phase I of I.02-11-040 on April 16, 2003. In Phase I of I.02-11-040, the Commission undertook investigation of activities of SoCalGas, SDG&E, their holding company (Sempra), and relevant affiliates as they relate to the 2000 – 2001 gas price spikes. In Phase II, which has not yet been scheduled, the Commission plans to address activities of Southwest Gas, Pacific Gas and Electric Company, and SCE related to the gas price spikes.

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<sup>2</sup> Unless otherwise indicated, all citations to sections refer to the Public Utilities Code and citations to rules refer to the Commission Rules of Practice and Procedure, which are codified at Chapter 1, Division 1 of Title 20 of the California Code of Regulations.

Phase I of I.02-11-040 has been bifurcated. Phase I.B, currently pending, has been scoped to address whether the non-utility affiliates of SoCalGas and SDG&E, or their parent company, played a role in causing the gas price spikes during the Subject Period, and whether concerns about affiliates or the parent's financial position caused SoCalGas and/or SDG&E to take actions that may have increased gas costs.<sup>3</sup>

Sempra and SCE have submitted prepared testimony in Phase I.B. Sempra's prepared Phase I.B testimony describes the role of Sempra's Energy Risk Management Department in the gas procurement activities of SoCalGas and SDG&E during the Subject Period and addresses Sempra's compliance with the Commission's affiliate transaction rules adopted in Decision (D.) 97-12-088 and D.98-08-035 and the Remedial Measures adopted in D.98-03-073 as a condition of the Sempra merger.

Without attempting to be comprehensive, a brief description of SCE's prepared Phase I.B testimony follows:

Chapter 1: Introduction and summary

Chapter 2: Background regarding Commission, Federal Energy Regulatory Commission, and U.S. Department of Justice reviews of the proposed merger that created Sempra, and the Remedial Measures that the agencies imposed on Sempra as a condition of authorizing the merger.

Chapter 3: Addresses SCE's view that the Sempra companies took steps to foreclose entry by competing pipelines into southern California.

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<sup>3</sup> Additionally, consideration of certain Phase I.A issues has been moved to Phase I.B because discovery responses were too late for inclusion in Phase I.A.

Chapter 4: Addresses Sempra's compliance with merger Remedial Measures and affiliate transaction rules.

Chapter 5: Addresses profits of Sempra's unregulated subsidiaries during 2000-2001.

The assigned Administrative Law Judge (ALJ) ruled at a February 6, 2006 PHC, with further detail in a February 21, 2006 ALJ ruling, that certain portions of SCE's prepared Phase I.B testimony would not be considered at this time, in particular the portions of Chapter 3 addressing Sempra's activities in Baja Mexico related to the Rosarito power plant, and other portions of the prepared testimony that address issues previously litigated in Phase I.A.

### **III. Background – I.03-02-033**

The Commission initiated I.03-02-033 on February 27, 2003 to evaluate the business activities of SDG&E, SoCalGas, Sempra, and relevant affiliates. The OII consolidated I.03-02-033 with I.02-11-040, due to the overlap with some of the issues in Phase I of that proceeding. In D.03-09-070, the Commission modified the OII initiating I.03-02-033 and, among other things, deconsolidated the two proceedings in part because of the divergence of their schedules.

In D.03-09-070, the Commission required an independent audit as the first step in I.03-02-033. The Commission directed that the audit be combined with the calendar year 2003 audit of affiliate compliance required by D.97-12-088 and D.98-08-035. D.03-09-070 provided direction for the combined audit, as follows:

An independent audit should be performed as the first step in this investigation, in order to assess the compliance of SDG&E, SoCalGas, and Sempra with relevant statutes and the Commission's affiliate transaction rules and whether the companies' business activities have posed potential problems or unjust or unreasonable impacts on utility customers. Because consumer interests go hand in hand with promoting competition, and consistent with the objectives of our existing affiliate transaction rules, the audit should

encompass potential conflicts of interest or activities that may be detrimental to competition. ...

The auditor should review Sempra's holding company and affiliate structure to identify any corporate relationships that may create potential conflicts between the interests of Sempra and the interests of the regulated utilities and their ratepayers. ...

The auditor should gather and analyze information on activities since December 17, 1997, when the Commission adopted affiliate transaction rules in D.97-12-088. The auditors may review activities prior to the audit period if they believe it necessary to fulfill the goals of the audit. The audit of compliance with the existing affiliate transaction rules should encompass 2003 activities (the calendar year 2003 audit), as well as activities in other years related to specific concerns that may be identified. In its audit report, the auditor should identify any areas and ways in which our affiliate transaction rules could be strengthened to prevent undesirable affiliate-related activities not addressed by the existing rules. (D.03-09-070, Ordering Paragraph 3.)

The resulting audit was overseen by Energy Division and undertaken by GDS Associates, Inc. In compliance with D.03-09-070, Energy Division filed the audit report in I.03-02-033 on February 28, 2006.

While the audit directed by D.03-09-070 was pending, Sempra commissioned its 2004 and 2005 affiliate compliance audits. The 2004 audit of SoCalGas and SDG&E was performed by NorthStar Consulting Group (NorthStar). Sempra submitted the NorthStar audit report for the two companies to Energy Division on May 2, 2005. Pursuant to an ALJ ruling, Sempra also filed the NorthStar audit report in I.03-02-033 on February 27, 2006. The 2005 affiliate compliance audit is being performed by Alliance Consulting Group (Alliance), with the audit report due to Energy Division on May 1, 2006. At the March 3 and

7, 2006 PHC, the ALJ ruled that Sempra shall also file the 2005 audit report in I.03-02-033.

#### **IV. Categorization of I.03-02-033, Ex Parte Rules, and Designation of Principal Hearing Officer**

In the OII, the Commission categorized I.02-11-040 as ratesetting, (Rule 6(c)(1); OII, page 8.) Persons had ten days to appeal. (Rule 6.4(a).) No appeals were filed, so the categorization of this proceeding as ratesetting is final. Ex parte communications in this investigation proceeding are subject to § 1701.3(c), Rule 7(c), and the reporting requirements of Rule 7.1.

In the OII, the Commission found that hearings are necessary in I.03-02-033, pursuant to Rule 6(c)(1). Some parties have questioned the need for hearings. In part because of the overlap with issues in I.02-11-040 requiring hearing, I confirm the need for hearings in I.03-02-033.

In a ratesetting proceeding, Rule 5(k)(2) defines the presiding officer as the principal hearing officer designated as such by the assigned Commissioner prior to the first hearing in the proceeding. In accordance with Rule 5(k)(2) and (l), ALJ Charlotte F. TerKeurst is designated as the principal hearing officer for I.03-02-033. The provisions of § 1701.3(a) apply.

#### **V. Scoping Memo for I.03-02-033 and Coordination with I.02-11-040**

The preliminary scoping memo included in the OII, pursuant to Rule 6(c)(1), identified the issues to be addressed in I.03-02-033. In D.03-09-070 modifying the OII, the Commission addressed further the intended scope of the investigation. The OII and D.03-09-070 identified the following issues to be addressed in this investigation:

1. Whether the business activities of SDG&E, SoCalGas, their holding company, and unregulated affiliates have complied with applicable statutes and the Commission's prior decisions, rules, and requirements.

2. Whether the business activities undertaken by the utilities and/or their holding company and affiliates pose potential problems or unjust or unreasonable impacts on utility customers.
3. Assessment of the potential for conflicts between the interests of Sempra and the interests of the regulated utilities and their ratepayers.
4. Assessment of potential conflicts of interest or activities that may be detrimental to competition.
5. Whether actions taken by SDG&E and SoCalGas, including the supply of natural gas, procurement of electricity, and construction of transmission lines, have been in the best interest of ratepayers or instead have been meant to benefit unregulated affiliates.
6. Whether current conditions contained in the holding company authorization decisions are adequate; and whether additional rules, conditions, or other changes are needed to protect ratepayers and the public.

At the March 3 and 7, 2006 PHC, procedural options for addressing the issues raised in the OII and D.03-09-070 were discussed. The ALJ and I ruled that, due to overlap with issues under investigation in Phase I.B of I.02-11-040, it is reasonable to have coordinated testimony and hearings in I.03-02-033 and Phase I.B of I.02-11-040 at this time. Following the PHC, SCE filed a proposed list of issues for the coordinated proceedings. SoCalGas, SDG&E, and Sempra filed comments on SCE's proposal.

It is reasonable to limit the scope of issues to be considered at this time to those that have already been addressed in the GDS and NorthStar audits and/or the testimony submitted in Phase I.B of I.02-11-040 that addresses related topics. This focused consideration is an expedient approach that will allow the identified issues to be considered in a timely manner. The prepared Phase I.B testimony to be considered at this time includes that submitted by Sempra, and

Chapter 2 and Chapter 4 of SCE's prepared testimony, except for the portion of Chapter 2 excluded previously.<sup>4</sup> If additional issues are raised in the 2005 affiliate compliance audit by Alliance to be filed on May 1, 2006, they may also be addressed. The remaining issues in I.03-02-033 and in Phase I.B of I.02-11-040 will be deferred at this time for later consideration in these or subsequent proceedings.

For each issue, the Commission will examine compliance with existing rules, requirements, and statutes. The Commission will also consider whether the companies' activities were counter to the interests of California gas and electricity ratepayers, benefited unregulated affiliates, impeded competition, or otherwise reflected conflicts between the interests of Sempra and the interests of the regulated utilities and their ratepayers. If valid concerns are found, the Commission will consider whether additional rules, conditions, or other remedies should be implemented.

Issues raised in the audits and/or the I.02-11-040 Phase I.B testimony to be considered at this time include, but may not be limited to, the following:<sup>5</sup>

1. Identification of covered affiliates and energy marketing affiliates for purposes of the affiliate transaction rules (Rules I.A, II.B and VI.B); whether the Commission rather than the utilities should make initial determinations regarding covered affiliates.
2. SoCalGas and SDG&E interconnect procurement activities with their liquefied natural gas (LNG) affiliates (Rules III.B.1, IV.B, and VII.I).

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<sup>4</sup> The February 21, 2006 ALJ ruling excluded one segment in Chapter 2 of SCE's prepared Phase I.B testimony: the last two sentences of paragraph 26 on page 2-9.

<sup>5</sup> Relevant affiliate transaction rules or Remedial Measures identified in the submitted documents are indicated parenthetically.



3. Whether SoCalGas and SDG&E should be required to modify recordkeeping, training, and evaluation procedures to ensure compliance with Rule III.
4. SDG&E trading practices (Rule III.B).
5. Transfer of noncustomer-specific non-public information and use of that information (Rules IV.B and V.E and Remedial Measures 6, 7, 12, 14, and 15); whether energy risk management should be prohibited as a shared service; whether SoCalGas and SDG&E should not be allowed to obtain energy market-related professional services from affiliates; whether there was inappropriate information sharing and/or decision making coordinated between SoCalGas and SDG&E; use of third-party telephone brokers by SoCalGas and SDG&E energy procurement groups.
6. Use of advertising disclaimers (Rules IV.C, V.F, and V.F.1)
7. Sharing of plant, facilities, equipment, or costs (Rule V.C); whether SoCalGas and SDG&E should reconfirm all affiliate shared service application users, conduct Access Management reviews, and keep documentation on file for improved management control.
8. Shared employees (Rules V.G.1 and V.G.2.e); whether temporary work assignments should be reported based on the ultimate beneficiary of the work; whether SDG&E should suspend and prohibit joint temporary employee assignments with its affiliates.
9. Whether SoCalGas and SDG&E should be required to develop written policies and procedures for each functional work group affected by the affiliate transaction rules.
10. Whether the Affiliate Compliance Departments of SoCalGas and SDG&E should be given more prominence, with an increase in their level of resources and positioning in the organizations.
11. Whether future annual compliance audits should be performed under the direction of Commission staff, rather than SoCalGas and SDG&E (Rule VI.C); whether SoCalGas and SDG&E should be required to develop written policies and procedures that address how outcomes and recommendations of each annual compliance audit will be reviewed.

12. Nontariffed products and services (Rules VII.D, VII.F, VII.H, and VII.I); data accessibility, business controls, accounting, auditing, and reporting practices; pricing relative to cost.

As directed at the March 3 and 7, 2006 PHC, parties are to meet and confer regarding issues that may require evidentiary hearings and still-pending discovery matters, and are to report the results of the meet-and-confer to the ALJ. The ALJ may issue a ruling regarding the scope of testimony and evidentiary hearings, if appropriate, based on the outcome of the meet-and-confer process. As ruled at the PHC, the evidentiary record developed in Phase I.A of I.02-11-040 will be available for the parties' use but the issues addressed in Phase I.A are not subject to relitigation during these coordinated proceedings.

## **VI. Schedule for Coordinated Proceedings**

The following schedule is adopted for the coordinated proceedings in I.02-11-040 and I.03-02-033, based on discussions at the March 3 and 7, 2006 PHC:

Meet-and-confer among the parties to discuss issues that require evidentiary hearings and remaining discovery issues	March 21, 2006
Parties notify ALJ via letter(s) regarding outcome of meet-and-confer	March 28, 2006
Scheduling conference call	April 5, 2006 at 4:00 p.m.
Sempra files Alliance audit report	May 1, 2006
Testimony by all parties responsive to GDS, NorthStar, and Alliance audits and allowed I.02-11-040 Phase I.B testimony	June 13, 2006
Concurrent reply testimony	July 18, 2006
Evidentiary hearings	August 1-11, 2006

Parties shall serve, but not file, all prepared testimony on the service lists in I.02-11-040 and I.03-02-033. A conference call has been scheduled for April 5, 2006 at 4:00 p.m. to discuss scheduling and other procedural matters. Parties may participate by calling 203-310-3009; the participant pass code is 487101. Evidentiary hearings will take place at the Commission Courtroom, State Office Building, 505 Van Ness Avenue, San Francisco, California, commencing at 10 a.m. on August 1, 2006.

The ALJ will set the briefing and submission schedule, taking into account the scope of the evidentiary hearings and the complexity of the issues involved, and may adjust the schedule in other respects as necessary during the course of the proceeding. Pursuant to Rule 8(d), parties requesting final oral argument before the Commission should include that request in their concurrent opening briefs.

Section 1701.5 provides that, in a ratesetting proceeding, the issues raised in the scoping memo are to be resolved within 18 months of the date the scoping memo is issued. I anticipate that completion of I.03-02-033 will occur within 18 months.

## **VII. Other Procedural Matters**

Service lists for I.02-11-040 and I.03-02-033 have been established previously and are available on the Commission's website. As indicated above, parties are to notify the ALJ if discovery disputes remain following the March 21, 2006 meet and confer. Other discovery and service requirements and Procedural Ground Rules are contained in the April 16, 2003 Assigned Commissioner ruling issued jointly in I.02-11-040 and I.03-02-033, which contains the scoping memo for Phase I of I.02-11-040.

Therefore, **IT IS RULED** that:

1. Ex parte communications in Investigation (I.) 03-02-033 are subject to Pub. Util. Code § 1701.3(c), and Rule 7(c).
2. The scope of I.03-02-033 and of coordinated proceedings to be held with I.02-11-040 is as set forth herein.
3. The schedule for the coordinated proceedings in I.02-11-040 and I.03-02-033 is as set forth herein, as further modified by the assigned Administrative Law Judge (ALJ).
4. Parties shall serve all prepared testimony in the coordinated proceedings on the service lists for I.02-11-040 and I.03-02-033.
5. A party may request final oral argument as set forth herein.
6. The principal hearing officer in I.03-02-033 pursuant to Rule 5(k) and (l) is ALJ Charlotte F. TerKeurst.

Dated March 21, 2006, at San Francisco, California.

/s/ GEOFFREY F. BROWN

Geoffrey F. Brown  
Assigned Commissioner

## **CERTIFICATE OF SERVICE**

I certify that I have by mail this day served a true copy of the original attached Scoping Memo for Investigation (I.) 03-02-033 and Assigned Commissioner Ruling Regarding Coordination of I.02-11-040 and I.03-02-033 on all parties of record in these proceedings or their attorneys of record.

Dated March 21, 2006, at San Francisco, California.

/s/ ERLINDA PULMANO

Erlinda Pulmano

## **N O T I C E**

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address to insure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.

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